

INDIANA HOUSING FINANCE AUTHORITY

MORTGAGE CREDIT CERTIFICATE PROGRAM

THE FEDERAL RECAPTURE TAX

The Mortgage Credit Certificate is funded from the proceeds of an IHFA Mortgage Revenue Bond. Therefore, Borrowers participating in the Program could be subject to the Federal Recapture Tax under certain conditions as discussed below.

Congress enacted legislation in 1988, subsequently amended in October 1990, to recapture some or the entire subsidy from homebuyers who receive qualified mortgage bond assistance after January 1, 1991. This includes all buyers who use IHFA mortgage loans and Mortgage Credit Certificates (MCC). The purpose of recapture was to receive the subsidy from homeowners who received rapid income increases after they purchased their home and, as a result, did not need the subsidy to remain homeowners. The Federal Recapture Tax on the mortgage under the Program is triggered when a disposition, usually a sale, of the financed residence takes place within nine (9) years of the purchase date. The amount of recapture that borrowers might have to pay depends on how much their incomes have increased, their family size at the time of sale, the original amount of the first mortgage, the length of time they owned their home and any gain realized on disposition of the home.

The borrower(s) is responsible for calculating and paying the recapture amount, if any, as additional Federal Tax Liability for the tax year in which the home is disposed. The amount of the recapture tax will not exceed fifty percent (50%) of the gain on the disposition of the home realized by the borrower(s).

No recapture tax is due if any of the following occurs:

- (a) The borrower(s) dispose of the residence later than nine (9) years after the mortgage loan is closed;
- (b) The home is disposed of as the result of the borrower(s) death;
- (c) The borrower transfers the home to a spouse or former spouse incident to divorce and no gain or loss was incurred on the transfer and included in his federal taxable income;
- (d) The home was disposed of at a loss; or
- (e) The Borrower(s) modified adjusted gross income for the year in which the home is sold does not exceed the threshold income adjusted for family size for such year. Modified adjusted gross income is calculated as follows:

Adjusted Gross Income from IRS 1040	\$	_____
Tax exempt income earned for the year	+	_____
Gain on sale of the home	-	_____
Modified adjusted gross income	=	\$ _____

There are several steps required to calculate the actual recapture amount owed. Adjustments may be made depending on the number of years the home is owned prior to disposition and the Borrower(s) income at the time of filing of the Federal Tax Return for the year of the disposition. The following outlines the steps involved in the calculation:

Threshold income (Adjusted Qualifying Income)

The threshold income is the maximum allowable federal income limit for the Mortgage Credit Certificate Program, for the area in which residence is located at the time the borrower was qualified for the Mortgage Credit Certificate Program. Each year of the nine (9) year holding period the threshold income is increased by 5% from the previous years' threshold income.

The threshold income for each of the nine (9) years is provided to the borrower(s) in the *Notice to Borrower(s) of Maximum Recapture Tax and of Method to Compute Recapture Tax on the Disposition of Home* letter.

Holding Period Percentage

The percentage is based on the year in which the disposition occurs after the loan closing date according to the following table:

Disposition within month of closing:	1 - 12	20%
	13 - 24	40%
	25 - 36	60%
	37 - 48	80%
	49 - 60	100%
	61 - 72	80%
	73 - 84	60%
	85 - 96	40%
	97 - 108	20%
	109 or more	No Recapture Tax

Maximum Recapture Amount

The federally subsidized amount, which is 6.25%, *multiplied* times the original amount of the first mortgage, *multiplied* times the holding period percentage.

Income Percentage

The modified adjusted gross income of the borrower(s) for the taxable year in which the disposition occurs *minus* the threshold income *divided* by 5000.

Adjusted Recapture Amount

The maximum recapture *multiplied* times the income percentage.

Recapture

Equals the lesser of the adjusted recapture amount or one-half the gain realized on the disposition of the residence.

Limitations and Special Rules on Recapture Tax

- (a) If you give away your home (other than to your spouse or ex-spouse incident to a divorce) you must determine your actual recapture tax as if you had sold your home for its fair market value;
- (b) If your home is destroyed by fire, storm, flood, or other casualty, there generally is no recapture tax if, within two (2) years, you purchase additional property for use as your principal residence or construct a new residence on the site of the home financed with your original subsidized mortgage loan;
- (c) In general, except as provided in future regulations, if two (2) or more persons own a home and are jointly liable for the subsidized mortgage loan, the actual recapture tax is determined separately for them based on their interests in the home;
- (d) Refinancing of the first mortgage does not result in a recapture tax liability. If the home is disposed of after the refinancing but prior to the original nine (9) year holding period recapture tax may be due. The holding period

adjustment for the period in which the first mortgage was outstanding would be used for calculating the recapture amount.

Within ninety (90) days from the date of the Final Approval IHFA will send to each borrower a *Notice to Borrower(s) of Maximum Recapture Tax and of Method to Compute Recapture Tax on Disposition of Home*. A sample of this notice is included on the following pages. Borrower(s) should keep this notice for future reference in calculating the recapture tax.